America's Foreign Loan Policy

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PLAYING the role of creditor nation is so new to America that she halts and stumbles in rendering the lines. Indeed the international audience wonders what the drama is all about. All we at home seem to know about it is that the rest of the world owes us a lot money, and in the matter of the Allied debt we are hopelessly divided as to whether or not it should be cancelled.

Thoughtful Americans realize, however, that whether we will or not this country must play a larger, a more helpful part in international finance. Though we decided, wisely or otherwisely, not to participate in the Genoa Conference that gathering of some two score nations called for the purpose of considering the economic restoration of Europe has again brought to the front the whole question of our foreign loan policy in relation to international rehabilitation. That we have thus far been without such a policy is painfully evident; that a stage in international finance has been reached where an intelligent and intelligible policy must be formulated seems equally obvious. Whatever the outcome of the Genoa Conference or of subsequent conferences of which it may be the forerunner, America's stake in its issue is profound and far-reaching. The

program of readjustment and economic rehabilitation adopted there, or elsewhere later, cannot overlook the supreme importance of America's attitude toward and interest in world reconstruction.

Conceding the wisdom of the Administration in declining to send official conferees to the Genoa meeting on the assumption that its agenda must necessarily involve questions of European politics in which we as a nation have registered an unequivocal decision not to mix, the stern fact remains that America of all the nations involved has, perhaps, most to gain or lose in the settlement of the economic questions there to be discussed. Wholly aside from motives of sympathy or sentiment, our direct self-interest as the chief creditor of the solvent, insolvent and bankrupt countries of Europe must give us deep interest and abiding concern in the problems and the outcome of the Conference.

The essential facts of the situation in which America finds herself as world creditor have been made familiar by frequent telling, and need be recited in outline only for the purposes of this paper. Examination of the international balance sheet shows that prior to the World War this country was in debt to the rest of the world, Europe mostly, in an aggregate (using round figures) of between three and five billion dollars. We were a debtor nation but with a so-called "favorable" balance of trade averaging about a half-billion dollars annually.

This comparatively small annual balance resulting from the excess of our exports over imports was settled

by payments made to foreign vessels fetching and carrying our foreign trade, for we had then only a relatively small merchant marine, apart from our coast wise and Great Lakes tonnage; by heavy annual payments to foreign insurance companies; by tourist expenditures and remittances by aliens resident in the United States to their home countries; and finally by occasional shipments of gold. With a free gold market prevailing practically everywhere gold was available at all times for international settlements. Thus peacefully the tide of trade ebbed and flowed year after year.

For decades a considerable volume of capital, estimated at three to five billion dollars, was invested and reinvested by the old surplus-capital nations of Europe in American securities and enterprises. Interest and dividend payments on this foreign investment account reduced correspondingly the annual balance in favor of the United States. (In passing it may be noted that even after civil strife had brought our industrial and commercial machinery almost to a standstill and plunged us into what at that stage of national development and income was a most burdensome national debt, Europe continued to extend us credit and to invest capital in our railways and other corporate enterprises. Nor was that flow of credit and capital abruptly terminated when we as a nation threatened to commit economic hari kari in the greenback paper money period). Always before the recent war we were a borrowing, a debtor nation.

And then came the great world cataclysm changing our international status almost over night from that of

a debtor to a creditor nation. When the war broke out we owed Europe four to five billon dollars. Now we are a creditor nation in an estimated total of twenty billions, more or less. Approximately one-half of this amount, or ten billions, is represented by the Allied debt, loans made by our Government to the Allied Powers during the war, which with interest accruals of about a billion more foots up a total of eleven billion dollars. The rest of the indebtedness of the outside world to America, much of which has been incurred since Armistic, has grown out of our excess of exports over imports and of advances in the form of loans to foreign governments, municipalities and corporations.

The world still remembers, and for the most part regrets, the period of feverish, unreal business "prosperity" which set in a few months after the close of the war. The waste and destruction of four years of devasting conflict left Europe economically enfeebled and in need of food supplies and raw materials with which to rebuild its shattered industrial structure. Neutral countries which had escaped the actual ravages of the war suffered scarcely less than the combatants from the breakdown of commercial intercourse, the derangement of business, domestic and foreign, and the burdens and inequalities that always inhere in a period of rapid inflation. America alone emerged from the ordeal economically vigorous and with resources unimpaired. To her the world turned for much needed peace supplies. For a few hectic months Uncle Sam enjoyed almost a monopoly of the international markets, selling for cash or credit the world around.

The flood tide of our foreign trade was reached in 1920 with exports valued at $8,228 million and imports of $5,278 million, making a total business of $13,506 million. Comparing these figures with the last normal pre-war year, when exports amounted to $2,363 million and imports to $1,894 million, it appears that the value of our exports in 1920 was 3½ times and of imports 2⅔ times that of 1913. In 1921 exports dropped to $4,485 million, a decline of 45 per cent compared with 1920, and imports declined to $2,509 million, a fall of 52 per cent. In comparing last year's total foreign trade with that of 1920, however, we are contrasting a year of enormously distended volume and highly inflated prices with one of relatively normal volume and greatly reduced prices. It should be noted that the value of our foreign trade last year though markedly less than that of the year preceding was far in excess of the best year before the war—exports being 90 per cent and imports 32 per cent greater than in 1913. Examination of these huge post-war totals, even after due allowance is made for higher unit values, leaves the foreign trade pessimist and the advocate of economic isolation with something to explain.

This enormous increase in our favorable balance of trade since the war, though a temporary situation perhaps, has brought us and the rest of the world some perplexing difficulties. The chief difficulty, for the purpose of this discussion, lies in the fact that a vast amount of our exports of recent years sold on open account remains unpaid for—"frozen indebtedness". The failure to liquidate this indebtedness to America is

due in the main to sheer inability to command the means of payment. In most European countries economic rehabilitation since the war has been painfully slow or wholly lacking. On the Continent every economic blunder known to history has been repeated and in Russia an entirely new experiment—new at least in its magnitude and thoroughness—has been tried out with disastrous consequences. Owing to their disordered and impoverished industrial and commercial affairs, their failure to impose adequate taxation to meet national budgets, their resort to printing press currency and to resulting instability and depreciation of the international exchanges, the economic status of most of these countries has steadily declined until today it is indeed desperate.

The outstanding obstacle in the path of trade resumption has been the uncertainty and the depreciation of the exchanges on America. The foreign exchanges of many countries, notably those east of the Rhine, have fallen to a mere fraction of their old par with the result that they cannot buy American dollars with which to pay for necessary imports. Some countries have had to resort to the primitive methods of barter and various make-shift expedients have been employed to carry on essential trade. Even those countries which have proceeded vigorously with the heavy tasks of internal economic restoration have found trade with America difficult owing to their inability to pay for American imports as formerly in goods and services. All of their invisible items of foreign trade have fallen off—the tourist business, immigrant re-

mittances, returns from merchant vessels and the rest. The export trade though increasing moderately in some instances with the promise of steady improvement, has in general fallen to discouragingly low levels.

In this situation the world has "swept the bottom of the barrel" to obtain the one universally acceptable medium of international payment, gold, to be sent to this country to pay for American goods. It is estimated that since 1915 gold in excess of $1,500,000,000 has been shipped to the United States. It has come mostly from European countries every one of which sorely needed the last ounce of it to sustain its greatly inflated paper currency and to stabilize or rectify its exchange. Nor does America either need or want the gold. We now have nearly three billion dollars of the yellow metal, roughly 40 per cent of the world's available supply. The combined reserves of the twelve Federal Reserve Banks stand at about 77 per cent as compared with 17 per cent for the Bank of England, and smaller percentages ranging down to nothing for the other central banks of Europe.

Indeed, it is a grave question whether our enormous accumulation of gold has not become a possible menace instead of a source of financial strength. In view of the recent reprehensible attacks upon the Federal Reserve System, of the attempts both within Congress and without to drag it into the maelstrom of politics, and of the vicious appeal to the unthinking and "economically illiterate" of cheap money or credit led by two outstanding figures in their respective fields, who have an addled conception of the fundamentals of sound currency and

credit, this great store of gold, which appears superficially to be "idle" might become under unwise legislation the basis for a renewal of disastrous inflation in this country.

As to the half or more of the foreign indebtedness to the United States represented by the Allied debt, we are not here primarily concerned. We are interested, vitally interested, in the solution of this vexed problem just as we must be profoundly interested in the early readjustment of the question of German reparations, or in the proposed loan to Germany. Economists, bankers and publicists continue to argue for and against cancellation of the Allied debt. The fact is that as matters now stand there is no wide-spread sentiment in this country favorable to cancellation. Furthermore, the whole question has been removed temporarily from the fields of academic discussion by the appointment, after months of endless and pointless debate in Congress, of the Foreign Debt Funding Commission charged with the task of solving this international problem. Though the stipulations and limitations prescribed in the Act creating the Commission would seem to foredoom its negotiations to failure, the task is theirs and the public must await the outcome.

Of more immediate and, perhaps, vital concern are those questions which cluster about the continuance of profitable commercial relations with the rest of the world. What can be done to thaw out our frozen foreign credits aggregating perhaps as much as our total annual foreign trade prior to the war? What must we do to insure a steady market abroad for our surplus

production greatly increased as a result of war time expansion? Shall we continue to extend credit to the outside world already heavily in our debt? Shall we adopt as a part of our international program the policy if importing foreign securities as well as goods? What is to be our policy regarding the investment of capital in foreign lands? Is it necessary or desirable to build up an investment market for foreign securities, and if so, how shall we proceed? Are we to go forward in the development of an open discount market for acceptances growing out of the export and import trade or shall we surrender the business back to London? What foreign loan policy shall be adopted to enable idle or part-time factories to go to work at full capacity? What, in short, is to be our foreign trade policy?

We have come to the place in our commercial intercourse with the rest of the world where we must choose between a policy of economic isolation and one of extended, continuous and systematic financial assistance to solvent debtor nations. The former course would involve contraction of production to the consumptive capacity of the domestic market with reduced industrial activity, the scrapping of a considerable part of our manufacturing and distributing equipment, recurring periods of business stagnation and continuous unemployment. To state the question thus is to answer it. The American business man, red-blooded but coolheaded, will not deliberately adopt a policy of contraction, stagnation and depression. He is going to fight this thing through and he is going to win!

A policy of "economic separateness' for this country advocated by some extreme nationalists is at once impracticable and indefensible. They urge that at best the foreign market does not take more than 10 to 15 per cent of our total production, and that since there is not enough liquid capital to finance Europe's needs and our own as yet undeveloped natural resources, it would be better to restrict our own capital to our own internal development. Admitting freely the dominating importance of domestic business and the urgency of adopting every sound measure to stimulate it to the utmost, it still remains true that foreign trade is an integral and essential element in our continued prosperity.

In all lines of production there is a portion varying from 10 to 20 per cent, the sale of which is necessary to the profitableness of the entire operation. As already noted our productive capacity greatly enhanced during the war is substantially in excess of the domestic market. Thus far our farms and fields have produced each year more than we needed at home, and in 1921 the export of agricultural products totalled more than two billion dollars, or a little over 50 per cent of our entire export business. Normally over 60 per cent of our raw cotton is sold abroad, nearly 50 per cent of our tobacco crop, 15 to 25 per cent (35 per cent in 1921) of our wheat, 13 per cent of our dressed meats, and so on with other farm products. As a result of our steady industrial expansion we had reached a stage even before the war where we were exporting each year a billion dollars worth of manufactured products. In many

industries it is now necessary to market abroad 20 to 30 per cent of the output in order that the works may be kept running and labor fully employed.

And it must be understood that if the 10 per cent of production that is sent abroad were shut off, domestic business could not continue upon a 90 per cent basis. In numerous instances this export of 10 per cent makes possible the economies of large-scale production and measures the difference between prosperity and dullness in the industry concerned as well as in other related industries. The fact should not be overlooked that behind every thousand dollar export of merchandise there are various domestic transactions preliminary to exportation several times the value of the export itself.

A casual glance at the leading items in our annual bill of imports shows, likewise, the fallacy of the notion that we can shut off commercial intercourse with the rest of the world. Each year we bring in from abroad some 250 million dollars' worth of coffee which to most of us has become a necessary of life, but which we never can grow within our continental borders; tea runs to 26 millions, cocoa 54, sugar 235, silk 200, hides and skins 200, and so on.

There is no longer room for discussion as to the importance of, the necessity for, foreign trade. The war and the post-war period threw foreign trade opportunities into our lap. But with the economic revival of our competitors a fierce contest for markets will ensue. We have got to fight hard, but clean, to retain and expand our foreign business. And we must keep steadily

in mind that in order to sell we must buy. To demand as sometime we may, the repayment of the Allied loans, or to expect the steady liquidation of the unfunded commercial debts of Europe to us, and at the same time to erect trade barriers which will make it impossible for the outside world to meet these obligations by sending us the only means of payment available to them, merchandise, would surely be the height of economic unwisdom.

The great outstanding problem of the world today is the restoration of the normal producing and consuming power of Europe, and whether she wishes it or not America is intimately and profoundly concerned in the solution of that problem. As the chief creditor nation, as banker and capitalist of the world, America stands in the place of the Europe of fifty years ago as the one possible source of capital and credit in sufficient volume to restore the world's broken economic structure. Europe's progress towards the correction of its unfavorable trade balance and the liquidation of its debts to America will be determined measurably by our willingness to assist her by further advances of capital and credit. In one form or another Europe must obtain long-term credits and the permanent investment of large amounts of American capital for many years to come.

The issue is not met by the little nationalist or the advocate of American isolation who reminds us that Europe already owes to American firms and individuals, apart from our gratuities to Germany through our speculation in marks, a huge total of floating debt, and that American industry needs at home all the capital it can

command. There is a shortage of real capital all over the world, but in the existing emergency we who have most must in our own self-interest share with those who have little or none. By force of circumstances growing out of the world's necessities and misfortunes resulting from the greatest of all wars, we have been placed in the position of a foreign investing nation before we were ready for that responsibility. These circumstances emphasize the need of a policy that will admit of a liberal attitude toward debtor nations and at the same time safeguard our own home interests.

Without having formulated any definite policy as to foreign loans we have in recent months absorbed a considerable volume of foreign securities. Figures presented by the Federal Reserve Board show that in the year 1921 over $650,000,000 of foreign loans were floated in the United States and about $500,000,000 in the first four months of the current year. In view of the fact that the importation of foreign securities has not been attended by any considerable outflow of gold, it is evident that the proceeds have been used to purchase American exports. This then is a class of imports which counts as much as any other in the restoration of the trade balance. Moreover, these invisible imports do not directly compete with other American products as sometimes is the case with visible imports, but serve American industry and agriculture by stimulating exports. Then, too, the importation of foreign securities has a decidedly favorable effect upon foreign exchange except as to those countries where depreciation is due primarily to inflation. This favorable effect has been

notably observable in the case of some recent South American loans. Each step in the improvement of the foreign exchange through the absorption of foreign securities provides the means for liquidating old obligations or placing new orders for export goods, which in turn tends to enhance both the consuming and the producing capacity of the debtor peoples. Every investment now made by us in foreign countries increases their ability to purchase the products of American agriculture, industry and labor.

The most familiar and striking example of the advantages of a national policy of foreign investments is, of course, that of Great Britian. For generations before the war vast amounts of British capital were invested in the industrial and commercial enterprises of other countries all over the world. Sir George Paish estimated the net amount of British capital invested abroad when the war broke out at $20,000,000,000. At 5 per cent the return upon these investments would amount to about a billion dollars annually. The balance of trade was always against her running in 1913 at about $650,000,000. Her imports each year exceeded her exports, yet her wealth increased, the exchanges were usually favorable to London, more gold flowed in than ebbed out, and London was the money market and financial power of the world. The explanation lies mainly in her enormous "invisible exports" of capital and of services in the form of shipping, banking and insurance. "The real significance of Britain's immense foreign investments as regards her national prosperity and wealth lies, however, not so much in the

actual income received from these investments as in the foundation which they have afforded to her constantly expanding foreign trade. Foreign investment has, in fact, been the corner stone of Great Britian's world wide trade".

Inspection of the figures of foreign loans floated in this country in the last sixteen months, totalling over a billion dollars, perhaps, shows that the great proportion of them consist of government and municipal issues. The recent flotation of the $10,000,000 Framerican loan to a leading steel concern of France and the 20,000,000 guilder Holland-American Line loan, the first large participation by American investors in securities of foreign shipping companies, anticipate the expansion of our foreign investment market to include foreign industrial and transportation securities. It took a great war threatening world destruction to teach the American people to invest largely in the obligations of their own Government. This experience prepared them to buy bonds of other governments. The next step in the process of investment education is to familiarize them with foreign securities based upon productive and distributive enterprise.

Assuming the most scrupulous care on the part of the investment bankers floating the loans to insure the soundness and productiveness of the enterprise concerned, this type of foreign security is no less safe than that of governments, and at the same time may be more immediately effective in contributing to the restoration of the international trade balance and the strengthening of our export business. London and Continental

bankers have in the past made such investments all over the world with direct, profitable returns to home manufacturers and exporters. For instance the investment of British capital in the railways of Argentina has resulted in large orders to English concerns for railway equipment and materials. In the earlier history of our country British investments in our railways had the same effect until our industries were developed to supply these materials. In the floating of foreign industrial loans, European bankers have in some instances arranged for a measure of participation by their nationals in the management of the industries thus financed, with the result that a steady flow of orders for materials has followed from the borrowing to the lending country. Though the maxim "trade follows the investment" is not to be interpreted too rigidly or universally, the experience of old investment countries has demonstrated its general logic.

It is not necessary here nor would it be profitable, perhaps, to enter into a discussion of the action of the Department of State in its letter of March 3 to American bankers laying down the principles which in its judgment should govern the placing of foreign loans in the United States. If it may be interpreted as a recognition by the Government, which in view of the prospective negotiations for refunding of the Allied debts and of the approaching international bank conference has a vital interest in the matter, of the fact that the time is at hand for considering the formulation of a national policy respecting foreign loans by the people of this country, then this action is timely and wholly commendable.

Nor is it necessary to discuss at length the proposition urged by some that no foreign loan should be floated in this country unless the borrower agrees to utilize the proceeds here. The fact is, however, as recently pointed out by Mr. Thomas W. Lamont, that "With America the heavy creditor nation that she is today, credits obtained here must necessarily be utilized here either by the borrower direct or by those to whom he assigns the credit." As another competent observer, Mr. George E. Roberts, states the case: "With New York exchange at a premium all over the world and gold flowing in this direction wherever gold is free to move, it is evident that none of the proceeds of loans made in this market are likely to be withdrawn from this country in any other form than that of our goods or products".

The fact that existing conditions require the final use of these credits in this country accords with the sound view that our available capital funds should be "utilized at this time in ways most practically helpful to American business interests and especially productive interests. That is where everybody wants them to be used, and the fact is that with interest rates and exchange rates as they are that is practically the only use that can be made of them".

There have been some cases, of course, where if goods had been purchased in the United States by the borrower, it would have resulted in exports of a nature that would have led to the continuous purchase of parts in the United States for years to come. It is not inconsistent with the general proposition outlined above

to suggest that bankers negotiating foreign loans should constantly seek to handle them in such a way as to further American trade and encourage in every legitimate way the expenditure of the funds in this country for exports.

The desolation of war has brought to America a new role as creditor nation, and with it a new opportunity and a new responsibility. An attitude of isolation from the world's perplexing economic problems is no longer possible. The rehabilitation of the torn economic structure of Europe and the restoration of order in world trade depend in large measure upon financial cooperation from America. We must learn to invest in sound foreign securities. As for generations England has done, we must get used to the idea of reinvesting at least the equivalent of income accruing abroad. If we have faith in the economic future of our country we must now while the opportunity is ours lay firm and secure foundations for the international trade of the future.

The measure and means of financial assistance which America can or should extend to other nations is predicated, of course, upon the recognition by those nations of their obligations and responsibilities. Not a dollar of American capital or credit should be used for political propaganda or militaristic purposes. American dollars are now all *peace* dollars. If and when European countries particularly shall establish political and social order, adopt a sound fiscal and financial program, stop printing paper currency, and introduce a rigid system of taxation and economy to enable them to balance their

domestic budgets, then the confidence of the American investor in their securities will be restored. Given these conditions, America must be prepared to cooperate liberally in the task of world restoration (1) by extending credit, including long-term credit to foreign customers who need our supplies, but must be given time in which to pay for them; (2) by a tariff policy which will make it possible and profitable for other countries to sell to us in order that they may buy from us; (3) by reinvesting at least the equivalent of income accruing abroad; and (4) by the development of an American investment market for foreign securities especially industrials and railroads.

This at least may serve to suggest what is meant by "A Foreign Loan Policy that will enable idle factories to get to work." The prospect challenges the highest type of American financial statemanship.